Westlock Grain Terminals
A Case Study

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Sponsors

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Board Members : (Back Row L-R) Wayne Peyre, Gil Dubrule, Richard Krikke, Steve Miller, Brian Trueblood, Lonnie Brown (Front Row L-R) Harry DeWindt, Dr Alan Watt, Denis Rivard, Larry Arndt

Westlock Terminals (NGC) LTD

Westlock Terminals (NGC) Ltd is an exciting new grain company incorporated on August 23, 2002 and began accepting grain on December 5, 2002. Westlock Terminals is an independently operated grain terminal located in the town of Westlock at the crossroads of highway 44 and highway 18, situated on a CN Railway main line.

Westlock Terminals Ltd is owned by over 230 shareholders that are a blend of farmers and business people from the draw area surrounding the terminal. Westlock Terminals provides regular returns to shareholders through the dividend yields of the Class “C” shares as well as the incentive yields of the Class “D” shares.

Westlock Terminals has utilized capital investment from the community to maintain a profitable operation. This commitment will facilitate the viability of local infrastructure in addition to providing investors a positive return on their investment. This commitment is evident in the organization’s “Mission Statement” and “Vision Statement” now and for the future.

Mission Statement

"To develop a viable broad-spectrum grain business, impacting community growth, promoting quality service and productivity."

Vision

"Your Grain Link To The Future"

The Westlock Grain Terminals is a very successful New Generation Co-operative located in Westlock, Alberta. In 2002, when the community found out that their grain terminal was going to be sold, they rallied together to raise more than $1.2 million to purchase the terminal as a community owned venture. Since then, the Co-op has paid healthy dividend, on its shares to members and investors every year and are following through on plans to continually expand their grain handling capacity. Its success was a result of the vision and dedication of a small group of farmers, with the support of some key individuals, and, as with any new venture, a little bit of luck. The experience of Westlock Terminals has lessons to offer to any community faced with the loss of a major economic asset.

Westlock Terminals and the Alberta Farm Crisis

The Westlock Terminal story is encouraging at a time when inspiration is hard to find in the rural Alberta countryside. In contrast to national impressions of Alberta as an oil rich petroleum state, rural sociologist Roger Epp claims that there are in fact 2 Albertas – one rich and one struggling – and that since 1996 these two Albertas have demonstrated "divergent spatial geographies and prospects." The first Alberta, an oil-rich and ranching province widely known across Canada "concentrated in the Highway 2 corridor linking Calgary and Edmonton, and also including the northern resource boom-towns of Fort McMurray and Grande Prairie." The second Alberta, a poorer and "spatially outer Alberta," he describes as rural, agricultural, and outside the "Alberta advantage".. It is this latter Alberta where Epp finds an ever deepening the farm crisis. As Epp explains:

> The farm crisis is about disintegrating rural communities. Rail lines are abandoned and grain elevators came down. Tax-bases shrink. Populations have aged and declined. Retail stores and government services like hospitals, schools and post offices are consolidated in larger centers. People, who have given volunteer energy, wear out or move away.
>
> The farm crisis is also about the lack of leadership that can represent a fractured agricultural community. It is about coming to terms with the national political irrelevance of the prairie farm vote, and with urban-rural tensions ripe for political manipulation. Farm people once were romanticized as the backbone of the country; now they are perceived as parasites on the public purse and feel powerless to change that perception.
>
> The farm crisis is about fears for the future of what is good work - work that feeds people, engages parents meaningfully with their children, and requires multiple skills. Now farm people talk about the prospect of becoming 'bio-serfs' under contract to one of a handful of seed-chemical conglomerates. They work great distances off the farm to subsidize their operations (in vulnerable rural professions like nursing), and face Revenue Canada reclassification as hobbyists for their trouble. They constitute perhaps the oldest occupational group in the country. Many of them are eating up what ought to be retirement equity, postponing what eventually will be a make-or-break period of generational transfer.
>
> In that sense, too, the crisis is about the immense psychological burden of keeping a third or fourth-generation family farm that is not merely a business, but a physical anchor of home and identity.
>
> Finally, the farm crisis is about an acute sense of government abandonment.

Se Roger Epp, The Farm Crisis. 2002. http://ualberta.ca/~parkland/post/Vol-IV-No1/03epp.html

In 2002, against this context of crisis, the farmers and communities of the Westlock region found a creative co-operative solution to save Westlock Terminals. Facing the farm crisis makes their achievement all the more impressive.

Background

The prairie grain elevator terminal is an iconic symbol of western Canada's agriculture roots, a community landmark whose height was challenged only by the church steeple. Virtually every Alberta community of more than a few hundred people had a grain elevator. Grain elevators were crucial for the survival of farming communities across the prairies, acting as the only market access point for their harvest every year. The terminals would buy grain from farmers, either for cash or at a contracted price, and then sell the grain again for international buyers or on the commodity futures market. To avoid the temptation of price gouging by the terminal owner, many of these many grain elevators were operated by farmer owned co-operatives, ranging from small community based co-operatives to hundreds owned by the Alberta Wheat Pool, Canada's first ever grain co-operative.

Over time, as transportation, primarily tractor trailer delivery improved and as grain prices receded in comparison to other commodities, larger, more centralized terminals were built and a series of grain handling company amalgamations took place. The Alberta Wheat Pool amalgamated with Manitoba Wheat Pool to form Agricore Co-operative. Finally in 2001, United Grain Growers Limited (founded in 1906) and Agricore Co-operative Ltd. amalgamated to become Agricore United ("Agricore"). Since then, small town grain terminal closures, coupled with the shutdown of a range of short-line railways across the province, has resulted in a general service decline. Farmers have been gradually pushed further afield to deliver their grain.

With over 1000 farms in Westlock County and direct access to approximately twice that number in surrounding counties, Westlock Terminals is located in the heart of one of the most productive grain growing regions on the continent. The county enjoys fertile soils and good balance of rain and sun. However, despite its proximity, by the end of the century many of the farmers in the region were selling their grain at surrounding terminals.

At the time, the then named Westlock "Agricore" elevator was handling approximately 85,000 tonnes of grain annually at a profit. For the company, however, these returns were not sufficient particularly in light of its hefty capital investment in upgrading the terminal's antiquated wood construction. Agricore was moving to close down the operations and to divert the majority of its customers to Edmonton terminals some 100 km away.

When the closure of the Westlock "Agricore" elevator was announced, a complaint (which, as with all such complaints, has been kept anonymous) went to the Competition Bureau (CB) Canada http://competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/home). The complainant raised concerns that the Agricore merger had reduced the competitiveness of grain handling in the Edmonton and Peace River Regions. Upon further review, CB agreed with the complainant and began talks with Agricore to resolve the issue. Agricore agreed to divest, rather than simply close down grain elevators in the Edmonton/Peace River region, including elevators in the communities of: Gaudin, Killam, Westlock, Bawlf, Rycroft and Falher. Agricore was given until August of 2002 to finalize the sale of the terminals.

Grain producers in the Westlock area affected by this decision of the CBA held a meeting to decide their next steps. The group of approximately 35 individuals created a three person committee (Dave Felstad, Randy Gabel, and Johann VonRennenkampff) to find a private buyer. The committee spent two months contacting large grain companies in Western Canada who might be interested in purchasing the facility. The producers understood that the terminal had been profitable for Agricore. They also realized the facility had two drawbacks:

1. There had not been substantial investments for decades
2. It was located in town, whereas most new terminals are located outside town centers to accommodate transport and growth.

Unfortunately, many private buyers thought that the terminals were simply too old and dilapidated for investment purposes. Slightly disheartened, the committee realized that a person or a group of people in the community were going to have to purchase the terminals. They had one year to solve the dilemma. They discussed creating a joint venture between five producers, based on models they had seen in other communities. However, these joint ventures tended to focus on the grain handling needs of the partners, rather than the wider farming community. They thus concluded that this should be a community initiative.

Dave Felstad presented their situation to the Westlock Rotary Club in an attempt to spark the interest of the local business community. There he was introduced to Marie Gallant of the Tawatinaw Community Futures Development Corporation (a not-for-profit organization committed to rural economic development - www.cfna.ca). Intrigued by the situation and understanding the importance of the terminals for the entire community, Marie requested a meeting with Dave and the other Committee members to talk about how she could help.

At their initial meeting, the committee stressed that losing the elevator would have significant economic and social impacts on the community. Marie could tell that they were very knowledgeable about the agriculture business, but lacked the necessary business planning experience. They decided to brainstorm different organizational forms they could create and the steps required to make them a reality. They indentified several business models that might work and decided to conduct additional research to evaluate their viability.

Based on some of the support provided by Marie Gallant, the steering committee was able to convince both the Town and the County of Westlock to contribute $5,000 each towards the costs of starting a new organization to own and manage the terminals. These funds were used primarily to support the prefeasibility work on the terminal, including trips to visit other community terminals, particularly in Saskatchewan. Trips to Saskatchewan were at the personal expense of the three founding Directors.

The group drew upon experiences generously shared by the buyers of Terminal 22 at Balcarres, Saskatchewan. Terminal 22, founded in 1998, is a modern state of the art grain handling facility that is "50/50 joint venture grain company comprised of local area farmers and Cargill Limited." (The Saskatchewan Encyclopedia) The Westlock group met with Terminal 22's Chair and Secretary Treasurer in April 2002 to discuss approaches for raising capital. They offered the following council:

- Keep share prices low enough to encourage investment from all members of the community, but high enough to raise sufficient investment capital.
- Set a short timeframe for people to invest (approximately six weeks) because the majority of investors will wait until the last week (or day) to purchase shares. If the timeframe is too long, investors may lose interest.
- Talk to the surrounding communities because they have a strong vested interest in this venture.
- Do not hire a salesman to sell the shares. This is the work of the project leadership. The people of the community will be more likely to trust someone they know and respect.

The committee returned to Westlock inspired and with renewed ideas for developing a successful community-owned terminal.

Building on the model of Terminal 22, the committee met with a few different lawyers about how to structure a publically held company that could sell shares to the community. They were struck by the amount of time and money needed to create a limited liability company, and particularly for meeting the Alberta Security Commissions disclosure process for issuing shares. They noted that costs of this model were quite high and this encouraged them to look at other models, which is when they encountered Brian Kaliel and Merle Good.

Brian Kaliel had been one of the few lawyers in the province with expertise in the co-op model. Merle Good was a tax specialist with Alberta Agriculture and Rural Development who had worked with a number of agriculture co-ops in the province through his extension role. Brian and Merle were among the key authors behind the revision the Alberta Co-operative Act. They had pushed for changes based on their experience working together on the formation of a number of co-ops. They pushed particularly hard on what they saw were limitations for co-operatives to raise capital. Based on their experience, they championed the inclusion of multi-stakeholder co-operatives (the Act had previously limited co-ops to one type of membership) and the inclusion of non-member investment shares, as well as the concept of the New Generation Co-operative (NGC).[1] New Generation Co-ops are sometimes described as hybrids

[1] The Alberta Co-operatives Act can be accessed on the Queen's Printer website: http://www.qp.alberta.ca/574.cfm?page=C28P1.cfm&leg_type=Acts&isbncln=9780779740185

of traditional co-ops structure and limited company. For a comprehensive review of the New Generation Co-op model, please See Appendix III: “New Generation Co-ops: Alberta’s Newest Option for Agriculture Business”.

In many ways, the Westlock Terminal Project was an ideal project for Brian and Merle. It encapsulated all the powers of the newly revised Act. Together and separately, Brian and Merle held a number of planning sessions with the Westlock committee to craft the co-op’s structure. In 2002, Westlock Terminals NGC became the first co-operative to be registered under the new Alberta Co-operative Act.

Though entitled Westlock Terminals (NGC) Ltd., Westlock Terminals also contains elements of the multi-stakeholder co-op. Principal among these is its ability to issue community member shares. This ability to issue various classes of shares proved to be crucial in its capital campaign. Founding members were able to generate considerable community engagement because the community locals would be the owners, allowing them to generate significant equity - something well-nigh impossible for a joint venture. In addition, share issues for co-operatives are not as onerous as they are for public companies (i.e., an offer of memorandum is used and a prospectus is not required). Consequently, shares can be placed for sale quickly and for less expense than shares for publicly traded corporations. For a more detailed discussion of the Westlock Terminals Share Structure, see Appendix I.

Having sorted out their legal structure, the group hired a business consultant from Edmonton, Serecon Consulting, to create a business plan. While the producers were able to capably estimate the financials regarding the receipt of grain, they had little experience with the shipping side, which was key to the co-op’s profitability. As well, the committee drew upon the expertise of an Agricore executive who drafted an interim budget (free of charge!) that included best case and worst case scenarios for the terminal. These scenarios indicated that the terminal would be a very lucrative investment if they had a good year, and that they would remain in the black even in bad years. The numbers were proof enough that the committee was talking about a promising venture, not an idle dream.

Forming a Board of Directors was the next major hurdle. The committee held a meeting in Westlock to update interested parties on the status of the initiative and to recruit more Board members. After some coercing and a little bit of humility, they were able to find 10 individuals to make a Board – two of whom were professionals from the business community. An even greater challenge for the founders was to fashion a “suite” of share issues that could connect the business interests with a range of local residents - farmers, professionals, the well-off, and the not-so-well-off – in order to maximize public buy-in.

The committee, working with advisors Brian Kaliel, Merle Good and Marie Gallant, spent a significant amount of time discussing the share process. They came up with the following:

- **Class A Shares**: Membership share for all members
- **Class B Shares**: A higher risk investment share that can be sold to members and non-members alike with an initial price of $2000
- **Class C Shares**: Investment shares that can be sold to both members and non members with priority redemption value and a fixed return of 7%.
- **Class D Shares**: Investment share that provides added returns to farming members who deliver grain
- **Class E Shares**: Share class for founding members used for initial co-op development costs.

Class 'E' shares were offered for sale to the founding members to cover the legal and consulting fees before a full share issue could be conducted. These shares were high risk. If the organization didn't start, they would lose their initial investment. If they were able to get the company up and running, class "E" shares were eligible to be converted into dividend paying shares at two to one, recognizing the risk of venture capital.

The Weslock Terminals committee estimated that they would have to raise at least $1 million to get the terminals up and running. Preferred, non-voting shares which were issued to the public were $5000 each, with an annual dividend of 7%. Producers could purchase shares for $2,000 for membership rights. They also had access to Class 'D' Shares which were $2,000 each and included patronage dividends and profits generated from grain handling.

The co-op made a strategic decision that it would be open to any delivery, whether or not the farmer was a member of the co-op. In this way they hoped to capture as much of the grain market in the region as possible. Limiting service to co-op members would likely deter many farmers from using the terminal. However, farmers who wanted to receive patronage returns (profit sharing based on the percentage of business conducted with the co-op) would be required to purchase a Class A membership Share. Class D Delivery Rights Share were also made available, so Class A members could receive greater patronage returns in proportion to the volumes they sold to the terminal.

Again, drawing on the sage advice from the experience of Terminal 22, the Board decided their initial share offering would be available for only 6 weeks from July, 2002 to August, 2002. They knew it was going to be an uphill battle. Local investors' confidence had recently been shaken by other failed agricultural initiatives in the region. For example, a number of farm families had lost money when a swine co-operative failed in nearby Barrhead. As well, a drought that same year deterred many producers from investing in the project. As a consequence, the Board focused more of its attention on raising capital from the non-farming community.

Many believe that many initial community investors based their decision to purchase shares on the reputation and leadership of the co-op Board whose members were respected, successful farmers and local business people. For others, the risk of the initial investment was offset by their desire to retain an important business in the community. These ranged from doctors and lawyers who saw the central role the grain terminal played in the community, to the owner of the farm implements store and tire shop, whose businesses would suffer from the closure of the terminal.

Clearly, the terminal would provide benefits to the surrounding communities. So, the committee drew up an agenda listing all the surrounding towns they were going to visit over the six weeks, finishing in Westlock. They made sure to inform all the community newspapers of their intentions and to spread the word. By this time, the committee was already generating positive print and radio media attention. The greater Westlock community was well versed in the project's rationale and leadership. To this day, the founders attribute much of their success to the crucial role the media played in supporting the project and its capital campaign.

Over the six weeks, the Board members pulled out all the stops. They held one-on-one meetings with community members, going over the business plan and memorandum of offering time and time again.

They presented their business case to the Chamber of Commerce and to the Rotary Club. They put ads in the paper promoting the shares and held investor registration meetings in each of the surrounding communities.

Despite these efforts, with one week remaining in the capital campaign, only 60% of the capital had been raised. Nerves and tensions were high. After almost a full year of effort, it wasn't until the very last week of campaigning that investors started to sign up. The team was able to raise $200,000 in the last week and $200,000 on the last *day* of the capital drive. This brought their total equity up to $1.2 million, exceeding expectations by over $200,000. (The founders believe that having a defined rate of return of 7% was important to the success of the preferred investment.)

After this impressive membership drive, they were able to incorporate on August 23, 2002 and purchase the terminal. Initially, Agricore tried to sell the elevator for $1 million. But with the deadline approaching, Agricore agreed to sell the elevator to WTL for $200,000.

Despite raising the necessary amount of capital, WTL still had a difficult time securing a loan with a financial institution. With $1.2 million in equity, the group sought a $400,000 loan to cover the entire working capital it would need for initial operations. Several attempts to access a loan from the large banks were unsuccessful. Eventually, based on the strength and reputation of its Board, WTL was able to do a deal with Alberta Treasury Branch (ATB). (At first two lenders had come forward: the Alberta Farm Services Corporation (AFSC) and ATB. However, due to continued wrangling between the two institutions over who had priority payback rights, the ATB assumed the whole of the loan. Dealing with one financier proved much easier than working with two.)

During the investment drive, Dave Felstad was in constant contact with the general manager, Bob Heck, from Prairie West Terminal. Bob was looking for a change and moving to Westlock brought him closer to his daughter and grandchildren. In September 2002 he moved to Westlock, bringing with him an immense amount of leadership and experience - not to mention past experience with a community run terminal. Bob understood the importance of having strong financial leadership and planning from the beginning, so he hired Stephane Gervais, a registered accountant, who brought to WTL the essential skills-set of a controller.

After WTL's first year of operations, investors received a dividend of 7%. Community shareholders were very pleasantly surprised. Many confessed to the Board that they had viewed their share investment as a write-off: " I saw it is a grant to a project, I never expected to see anything back." Since the dividend was issued just when holders of stock-market shares, mutual funds and RRSPs suffered terrible losses, the Board had less difficulty issuing a second share offer to finance WTL's expansion, including an expansion of its rail line, a new steel terminal, and an additional steel bin as well as cleaning capacity. All of these upgrades would improve efficiencies and enhance the value of the grain. This is the third of four expansion plans and will be completed by the late fall or early winter of the 2009-2010 crop year. A final infrastructure expansion phase is planned to begin in 2012.

Currently, WTL is owned by 239 shareholders, a blend of farmers and business people, predominately from the area surrounding the terminal. Westlock Terminals provides regular returns to shareholders through the dividend yields of the Class "C" shares as well as the incentive yields of the Class "D" shares.

WTL's current growth stands at about 15% per year: a significant turnaround for a terminal that was deemed substandard and only marginally profitable under Agricore's control.

The Board is almost as diverse as the membership, comprising individuals with a broad range of backgrounds. They agree that it is in the best interest of all stakeholders to ensure the business is profitable, progressive and gives back to the members. Unlike private corporations in which one or two individuals drive the process, the co-operative Board needs excellent leadership and a "reasonably coherent" Board of Directors. The Board goes to great lengths to nominate new Board members who have good strong leadership and a diverse skill set including business planning, accounting, investment, farm management, and grain shipping.

WTL has utilized capital investment from the community to maintain a profitable operation in Westlock and to even upgrade and expand operations and facilities. This commitment facilitated the viability of local infrastructure, ensured continued rail connections, and in addition provided investors a positive return on their investment. Their rapid growth contrasts sharply with the experience of other grain terminals across the prairies.

The Competition Bureau had required that Agricore sell, not close, six terminals in the prairie regions, including the Westlock terminal. Unfortunately, the terminals in Rycroft and Falher, while sold initially to farmer groups, have since shut down. The Bawlf elevator has been purchased by ConAgra and is focused exclusively on malt barleys. Guadin and Killam continue to operate under locally owned, limited liability companies: in Killam, Great Northern Grains, and in Gaudin, Providence Grain. A future comparative study on the advantages and disadvantages of the co-operative and the limited liability company, in three communities with relatively similar contexts, would be very revealing.

Role of intermediaries

The Westlock group benefited from the support of Marie Gallant, the then Executive Director of the Community Futures office. Marie played several key roles:

- Helped with brainstorming and developing the business concept.
- Believed it was a viable venture and offered encouragement whenever possible.
- Helped construct the Board.
- Assisted in dealing with lawyers, insurance companies and financial institutions and Marie's background in commercial banking helped secure financing.
- Kept the media, Rotary Club and Chamber of Commerce involved at all stages.
- Offered administrative support, such a meeting room and photocopying services.
- Knew to step out when they organized a competent Board and general manager.

Westlock Terminals also benefitted significantly from the support of Merle Good, a tax specialist from Alberta Agriculture and Rural Development and Brian Kaliel, a government agriculture tax specialist and corporate lawyer with expertise in the co-operative model. As mentioned, Merle and Brian had worked closely together in helping to draft the Alberta Co-op legislation which provided for New Generation Co-ops. Working with the steering committee together and singularly, they helped guide WTL to become the first example of a New Generation Co-op under the new Alberta legislation.

SOME COMPARATIVE ISSUES

The Experience of Beiseker, Alberta

The situation of the community of Beiseker, Alberta is similar to that of Westlock in many respects. Viterra, a large, diversified Canadian grain handler that originated in the merger of the Saskatchewan Wheat Pool and Agricore-United, closed down the terminal in Beiseker. This obliged producers to travel to other towns to deliver grain. The current terminal is in good shape and local farmers would like to buy it, but Viterra is unwilling to sell. It will be interesting to watch how Beiseker overcomes its challenges.

There are also some very interesting differences between Westlock and Beiseker. For Beiseker:

Pros	Cons
• Good grain mix and tonnage, with production tonnage similar to those of the Westlock area. Beiseker is one of perhaps only two or three areas in Alberta where an independently owned grain terminal like Westlock's would be viable. • Significant gap in service to the east of Beiseker. • Current facility is good shape, mostly steel bins. • Good access to rail lines. • Motivated group of producers with, interestingly, a surprising number of younger farmers when compared to Westlock.	• Viterra does not have to sell the facility, as Agricore was obliged to sell the Westlock elevator by the CB. • There are several options: they can try to purchase terminal again, build another terminal, or create a producer car delivery system. • There is no set timeline, reducing the sense of urgency that drove developments in Westlock. • Smaller core community. While Westlock drew its membership from surrounding smaller communities, the core of its membership is from the immediate Westlock area. Beiseker may have to draw members from a wider area

The Westlock Co-op Board Model

The Westlock Terminal Board model has been criticized by some other co-operative boards because it does not pay compensation to its board members. Many WTL Board members believe that a voluntary Board is very important to the co-op's success. They feel that individuals committed to the co-op only require small yearly per diems, paid only if the organization is financially successful over the fiscal year.

Representation from all share types is included on the WT Board to maintain equal representation. A minimum of six members of the Board are elected by the producers who deliver grain to the elevators (Class 'A' Shareholders). In addition, 40% of the Board must be elected and/or appointed by community investors who do not hold voting power (Class 'B' and 'C' Shareholders). As a result, the Board is made up of professionals and farmers from the community.

Board members can sit on the Board for a maximum of six years (three full terms). Election to the Board is staggered so there are always new and old members. They recognize that six years is a short time to sit on the Board but believe having new Directors helps the Board, its members and employees stay focused.

Opportunities and challenges for replication

There is a clear contradiction in attempting to replicate a co-op – it is impossible to replicate the exact economic and social conditions and context that gave rise to WTL. There were several important milestones that makes WTL a unique example and difficult to replicate. One of the most important was that Competition Bureau Canada required Agricore to sell the grain elevator (See original decision here http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/00387.html). As a result, WTL was able to purchase the elevator for a fraction of the asking price. Also, organizers were able to secure a loan with ATB because of the strength and reputation of the initial Board members. Lastly, the Board's ability to raise capital in the initial share issue is indicative of the strong community support the co-op enjoyed.

What Worked For Westlock

While WTL may not be replicable, there are some transferable lessons:

a. Tenacious leadership is needed. Identify leaders and give them as much support as possible.
b. Make certain the founding members have the community support necessary to raise sufficient capital.
c. Determine how much you want this co-op. Will the significant sacrifice be worth the effort?
d. Identify what you know and, more importantly, what you don't know about your business. If there is an area you are unsure of, find an expert within the community and get him/her involved in the decision-making process.
e. Examine all the options for raising capital. Will businesses, municipalities, and/or individuals invest? If there are only a few major investors, the co-operative model may not be the best option.
f. Examine opportunities for alliances with other businesses and co-operatives if it builds the business case.
g. Seek seed capital from municipal and county governments.
h. Tour other community-owned initiatives.
i. Get an independent party to evaluate the business opportunity.
j. Set a reasonable timeline.
k. Board should sell shares to gain community support.
l. Get media and business groups like the Rotary and Chamber of Commerce involved in the early stages. Keep them informed throughout the entire process.
m. Identify businesses in the community that will be impacted by the success or failure of your organization, and get them involved.
n. Be astute of legal advice about co-ops. Not all lawyers understand potential co-operative structures thoroughly. Find a lawyer with co-op experience.
o. Initial Board members must believe in the co-op and be willing to purchase some of the first share offering to cover start up costs.
p. Hire competent, experienced, and motivated management (including an operations manager and financial controller).

APPENDIX I: COMPARISON OF SHARE CLASSES

Under the new Alberta Co-operatives Act of 2001, different classes of shares became possible. WTL established a share structure that enabled it to access investment capital from the broader non-farming community. As WTL was the first co-operative to use different share classes under the new legislation, the group had to forge new ground. Five categories of shares were created. Each class has implications for the others. It was a challenge determining the classes and their structure. See Alberta Co-operatives Act at http://www.acca.coop/ABCo-operatives.pdf

Share pricing requires knowing how much capital needs to be raised and understanding the audience that is expected to buy. As a founding Board member noted, "You don't want to set the price too high. You need confidence that you are not getting too much money but only what is needed.... You need to determine how much capital is needed and how many people there are to draw from."

Another issue to address is the rights of shareholders in the event of the co-operative's dissolution.

> When starting, people are most concerned as to what happens if you fail. But they should also be concerned about what happens if the organization succeeds. (Board Member Interview)

A synopsis of the share structure follows. Also see Appendix III: Comparison of Share Classes.

Class 'A' Shares
Only holders of these shares are members of the co-operative with the benefits that attach to co-operative membership (i.e., one member, one vote; eligible to stand for election on the Board; the member's share of profits is based upon the value of grain delivered to the terminal over the fiscal year). Furthermore, delivery contracts are only available to those with Class 'A' Shares (although non-members may also deliver without the aforementioned member rights). Consequently, members are grain producers. Class A shares set at $2000 and a member can hold only 1 Class 'A' Share. Members who wish a share of profits based on delivery of grain are offered Class D Shares for this purpose.

Class 'D' Shares
Only those who hold or are approved to hold Class 'A' Shares may purchase Class 'D' (or Delivery) Shares. If the Board so directs, there may also be a requirement that the Class 'D' shareholders have entered into delivery rights contracts with the co-op.

In WTL, delivery rights and obligations were not attached to shares (as is the case in some new generation co-operatives). However, the ability to realize patronage refunds[2] on larger volumes of grain delivery to the co-operative is enhanced by the ownership of additional Class 'D' shares. To accomplish this, the holders of Class 'D' shares are entitled to receive a surplus in proportion to their share of business with the co-op once the Class 'C' shareholders (see below) have received their dividends. More Class 'D' shares entitle the shareholder to surplus on larger total deliveries to the co-operative. WTL is limited to pay a patronage dividend up to 25% of original investment of the Class "D" shareholders.

[2] Patronage refunds in co-operatives are a share of the surplus the co-operative realizes at the end of the fiscal year. They are distributed back to members in proportion to each member's individual use of the co-operative.

Class 'E' Shares
Shares were issued to raise funds for development of the co-operative (e.g., fees for legal counsel, initial costs of hiring a general manager). The budget for these development costs was $120,000. 120 shares were offered at $1,000 per share.

As the Class 'E' shares were sold when the co-operative concept was just being developed, the Board determined that a later conversion (within one year of registration of the co-op) would provide a 2 for 1 value for these shares in recognition of the associated risk. In other words,

- One Class 'E' share could be converted to one Class 'B' share (@ $2,000 per share); or
- One Class 'E' share could be converted to one Class 'D' share (@ $2,000 per share; the share holder must be qualified to hold Class 'D' Shares); or
- Five Class 'E' shares could be converted to two Class 'C' shares (@ $5,000 per share).

Along with Class 'C' shares, the Class "E" shares would have priority in the event of the co-op's dissolution. However, all class 'E' shares have since been converted to either Class 'B' or 'C' shares as outlined above. As Class 'E' shares were used to raise the very high-risk capital used for the start-up of the co-op, there is no intent to issue these shares again.

Class 'C" Shares
The Board recognized that it was important to have preferred shares to raise capital as they will attract more investors than common shares. Accordingly, in the event of the dissolution of the co-operative, following the payment of primary debt, Class 'C' shares would have priority payout status.

Setting the value of the shares required understanding how much community people would pay. Shares were issued at $5,000 each. "Some people bought one 'C' share and hoped that the co-operative would be successful. But they were prepared to take the risk [that it wouldn't]. Others looked at the people behind it and believed that they knew what they were doing." With an initial target of $1 million, 200 par value voting Class 'C' series 'I' were offered and sold.

Setting the dividend rate for the preferred shares was challenging. (Deliberations required three meetings to set the rate and determine if the return should be cumulative or non-cumulative.) The Board determined that 7% was a reasonable rate of return for the risk involved. A lower rate would not attract investors; while a higher rate would be onerous for the co-op. As one Board member put it: "At 7%, money leaves the stock market to go into banks; at less than 7%, money goes into the stock market." This was the Board's assessment in 2002. With lower current (2009) interest rates, the investment would look even more attractive.

The Board may decide not to pay out a dividend or a portion of a dividend for Class 'C-I' shares in any given year. However, if the entire dividend is not declared, shareholders accumulate the right to the outstanding amount of dividends due. Such amounts shall not compound until declared. If dividends were not paid within the first five years of the co-operative's registration, holders of 70% of the Class 'C-I' shares could have called for a retraction of the Class 'C-I' shares or for the co-op to acquire the shares at the par-value plus declared but unpaid dividends.

These shares were available to members and non-members.

In accordance with the Alberta Co-operatives Act, Class ‘C’ shareholders may elect 20% of the Board of Directors. Other voting privileges of Class ‘C’ shareholders along with other investment shareholders are restricted to specific circumstances, as defined in the Co-operatives Act, such as those requiring one or more changes in the WTL Articles of Incorporation.

Class ‘B’ Shares

These growth shares are tightly tied to the co-operative’s success. They therefore produce the highest return and have lower priority than do Class ‘C’ in the event of dissolution. As one of the founding Board members noted, “’B’ Shares make the most money; but ... you can’t cash in.” They trade at market value. These shares were available to members and non-members.

The initial Series ‘I’ of Class ‘B’ shares were issued at $2,000 each. Dividends are determined by the Board of Directors and may vary from year to year. Initially, the rate of return on dividends was made equivalent per share with Class ‘A’ shares. However, the articles tying Class ‘B’ shares to Class ‘A’ shares were eliminated subsequently by the Board. It reasoned that members who want to participate in the growth of WTL should purchase Class ‘B’ shares.

‘B’ shares were the most difficult to value. A formula for valuation would have been very helpful.

APPENDIX II: COMPARISON OF SHARE CLASSES

	Class A Shares[3]	**Class B Shares**	**Class C Shares**	**Class D Shares**	**Class E Shares**
Purpose	Determines who has membership and who has delivery rights.	Investment shares	Investment shares	Investment shares that provide added returns for delivery	Investment shares that funded costs of co-operative development
Available to members only, non-members, or both?	Members only. Only one share per member.	A series may be issued to members, non-members, or both.	A series may be issued to members, non-members, or both.	Members only (must hold or be approved to hold Class 'A' shares and may require entry into delivery rights contracts)	No
Par or Non-par value?	Par-value	Non-par value	Par-value for 'C-I' Shares	Par-value	Non-par value
Issue price	$2,000	$2,000 for initial series 'B-I' shares	$5,000 for initial series 'C-I' shares	$2,000	$1,000
Maximum number of Shares issued		Unlimited in Class 'B'. Directors may fix a number within series subsequent to the 'B-I' series.	Unlimited in Class 'C', but 'C-I' series limited to maximum of 200	Unlimited number of shares	Maximum of 120 shares
Transferable?		Transferable	Transferable		
Returns	Share equivalent Class 'B' shares.	Dividends as may be declared by the Board from time to time. Shares equivalent with Class 'A' shares.	For 'C-I' series: 7% of price. Dividend paid if declared by Board. If not declared or not fully declared, rights to outstanding annual dividend accumulates, but not at a compounded rate	Participate in surplus of goods and services sold by shareholder to co-op after payment of dividends to holders of Class 'C'	Non-accumulative dividends as declared by Board from time to time
Rate for redemption/ acquisition of shares by co-op	At par value	At $2,000 or higher as may be determined by the Board from time to time, plus all unpaid declared dividends.	At $5,000 plus all unpaid declared dividends and all undeclared accumulated dividends.	At price paid therefore, plus all unpaid patronage dividends declared thereon.	

[3] No information provided on "Investment Share Capital" document.

	Class A Shares[3]	Class B Shares	Class C Shares	Class D Shares	Class E Shares
Limitations of redemption/acquisition of shares by co-op	Redeemed by co-op within one year of revocation of membership	Only after five years elapsed since issuance. No obligation to acquire more than 10 Class 'B' shares annually.	Only after ten years elapsed since issuance or if there have been no dividends paid on shares in first 5 years. -If no dividends have been paid, within 5 years of co-op incorporation, a vote of 70% of Class 'C-I' shareholders may require co-op to retract or acquire shares and declared but unpaid dividends. -If dividends paid within 5 years, no right of redemption or retraction until 10 years after registration date, at which time, there is no obligation for co-op to acquire more than 10 Class 'C-I' Shares annually.	An unlimited number of $2,000 par value non-voting Class "D" Shares issued only to members and designated as class of investment shares pursuant to Section 427 of the Co-operatives Act (Alberta) (the Class "D" Shares) If any Class "D" shares are redeemed, they shall be redeemable at the par value plus all unpaid patronage dividends declared thereon.	Converted into B, C or D within a year of the co-op's incorporation
Voting rights	Voting	Limited voting	Limited voting	Non-voting	Non-voting
Board representation	Elect all Board except those representing Classes 'B' and 'C' shareholders when applicable.	Class 'B' shareholders as a whole have the right to elect 20% of Directors	Class 'C' as a whole has the right to elect 20% of Directors	None	None
In the event of dissolution			Paid out rateably with Class 'E' shares and in priority to Classes 'A', 'B', and 'D' shares	Paid out rateably with Classes 'A' and 'B' shares after Classes 'C' and 'E' shares	Paid out rateably with Class 'C' shares and in priority to Class 'A', 'B,' and 'D' shares
Others					-Convertible within one year of Co-op's registration to: Class B at 1:1 Class D at 1:1[4] Class C at 5:2

[4] Provided shareholder has a Class A share and otherwise qualifies for Class D shares

Appendix III: New Generation Co-ops:
Alberta's Newest Option for Agriculture Business

A BASIC OUTLINE:

NEW GENERATION CO-OPS; ALBERTA'S NEWEST OPTION FOR AGRICULTURAL BUSINESS

Based on a Seminar presented by Brian P. Kaliel for Alberta Agriculture and Rural Development on December 3, 2002

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- Business Corporations
- Partnership/Joint Venture
- New Generation Cooperatives

2. Be Objective and Dispassionate About Choosing a Model - Pick the Model Which Makes the Best Business Sense

- De-politicizing NCGs/The Corporate Name Issue (eg: "NCG", "Group", "Association", rather than Co-op or Limited).

3. NCG vs. Business Corporation
NCG vs. Partnership/Joint Venture

The Key Issues:

- Control:
  - Producer/Members or Investors
  - "One Member One Vote" is not the end of the story
- Raising Capital:
  - Whether an NCG, or a business corporation or a partnership/joint venture is best will depend on the circumstances in each case
- Tax Issues:
  - eg: Is patronage flowthrough an issue?

4. NCG vs. Traditional Co-op

NCGs better suited if:

- Limited Membership/Producer Control an Issue
- High Capital Contribution Per Member Required
- Delivery Rights Contracts Involved
- Increase/Maintenance in Share Value/Investment an Issue

- Producers wish to pool/raise capital to aggressively pursue a business opportunity which will yield additional profits to their individual operations; and are interested in an investment which may increase in value.

5. **"Legal" Differences Between NCGs and Traditional Co-ops**

NCGs:

- Agricultural Use Only
- Must Issue Member Shares and Shares for Patronage Rights - Shareholder Value Tied to Share Capital
- Name Flexibility
- Ability to Issue "Designated" Shares Connected With Delivery Rights/Patronage Dividends
- More Flexibility for Redemption Rights/Share Transfer Rights Through Bylaws

The main difference is in how NCGs are used. The *Cooperatives Act* gives all Cooperatives the ability to restrict membership (different than Saskatchewan, Manitoba and Canada legislation).

6. **Prime NCG "Situations"**

- Capital:
  - Where the ability/need to raise significant amounts of capital from producer members is an issue.
  - Where community support to raise capital for a "rural development project" is an issue.
- Value Added Projects/Producer Control:
  - Where producers which to control marketing and processing of their products and receive value added returns.
- Diversification/Innovation:
  - Where there is no exiting business or service to meet producer needs, and producers wish to pool resources to create new markets or ventures.

B. GETTING ORGANIZED - PRE-INCORPORATION STEPS

1. The Organizational Personnel

- Organizing Committees
- Paid Organizers and Consultants
- Key Issues: - Avoid "Burn Out" and Loss of Focus
  - Qualified and Knowledgeable Management

2. The Business Plan

- The Crucial Question - Knowing Exactly How the Project is Going to Make Money For You.
- Consultants/Feasibility Studies and Your Particular Project.
- May be Required for Offering Memorandum and Due Diligence.

3. Consider the Use of A Society For Pre-Incorporation Steps

- Government Funding.
- Society Documents Should Provide For Transfer of Assets to NCG.

4. Determine Capital Requirements

- Minimum Approximately 50%
- How Much?
- From Whom? Define Your Potential Investors
- How - What Type of Share Capital (eg: Membership; Investor; Designated; How Many Classes; Conversion Rights; Redemption Rights; Options; Preferences; Returns; etc.)?
- Is RRSP eligibility an issue?

5. Determine Seed Capital Requirements

- How much?
- What Mechanism (eg: Loans, Convertible Shares, etc.)?

- Seed Capital Agreement

6. **Financing Requirements**

   - Ensure Financing Will be Available if Capital Raised.
   - Discuss Lending Terms. Consider Setting A Conditional Commitment.

7. **Governance and Control Issues**

   - What model is best suited to the proposed members/shareholders/ investors.
   - Is Producer Control Essential?
   - Will Other Investors Require Control Based on Amount of Investment?

8. **Timing Issues**

   - Develop a Time Line for the Project

9. **Legal and Tax Advice**

10. **The Last Step: Choose the Organizational Model Which Best Suits The Project**

    - Be Prepared to Be Flexible. It's Okay to Change Your Mind.

- honesty, skill, insurance, indemnity

- Shares, Membership and Transfers:
  - Qualifications, classes of shares, applications for membership, right to refuse membership, transfer and transmission of share, duty of members, withdrawal of members, termination of membership, redemption of shares
- Allocation of Revenues:
  - Disposition of surplus, patronage dividends, borrowing, purchase of share capital
- Delegates:
  - Right to vote through delegates
- Meetings of Members:
  - Annual meeting, notice, place and time, voting procedure, special meetings

C. INCORPORATION

1. The Incorporation Documents

- Articles of Incorporation

  - name
  - registered office and business address
  - names and addresses of incorporators (at least 3) (important - first directors: sign initial corporate documents, offering memorandum, etc.)
  - minimum and maximum number of directors
  - restrictions on business (NCG's - agriculture)
  - objects and purposes of cooperatives
  - restrictions on powers of directors
  - "Cooperative" basis
  - capitalization [VERY IMPORTANT]
  - maximum interest rate on member loans
  - restrictions on transfer of member interest

- Notice of Registered Office

- Notice of Names & Addresses of Directors

- Incorporators' Declaration re: Section 2 (Cooperative Basis)

- Incorporators' Declaration re: Part 18 Division 4 (NCG Provisions)

- NUANS name search

- Filing Fee ($100.00)

2. The Result

A body corporate with a Board of Directors (the original Incorporators) who can carry through with the important remaining steps.

NOTE: STEPS TO BE TAKEN NEXT WILL VARY WITH EACH PROJECT

D. POST-INCORPORATION DOCUMENTS (THE SUBSCRIPTION PACKAGE) - RAISING THE CAPITAL

1. Subscription Agreement/Membership Application

- Securities Compliance
- Types and Numbers of Share Capital Applied For
- Covenants

2. Offering Memorandum/Prcspectus

3. Risk Acknowledgment

4. Delivery Rights Contract

- See Section F

5. Unanimous Agreement

- A Unanimous Agreement may require a greater number of votes for directors or members, or investment shareholders, to effect an action, than is required by the Act. s. 5(3)

6. Proposed Bylaws

- General Conduct of Business: - Use of corporate seal; fiscal year; execution of instruments; business to be conducted by Board; information available to members.
- Directors: - Number of directors, election of directors, apportionment of directors, quorum, qualifications, removal, vacancies, electronic meetings, written Resolutions; notice time and place of meeting, officers, votes to govern, conflict of interest.
- Committees and Officers: - Powers and duties, terms of employment, auditor, bonding requirements.
- Duty of Care and Protection of Directors and Officers:

E. POST-INCORPORATION - COMPLETING CAPITALIZATION TO FIRST MEETING OF MEMBERS

1. **Has the Capitalization Threshold (and Other Conditions) Been Met?**

    - Release of Capital

2. **Share Issue**

    - Directors Review and Accept/Reject Share Subscriptions

3. **Financing/Project Acquisition Issues**

4. **First Meeting of Member Shareholders (180 Days)**

    - Adopt Bylaws
    - Elect First Board (Minimum 60%)

5. **First Meeting of Investor Shareholders**

    - Elect Directors (Maximum 20%)

F. DELIVERY RIGHTS CONTRACTS

1. Checklist of Common Issues

- Sale/Purchase Obligations:
  - Amount (units) member entitled to sell/NCG obligated to purchase
  - Relationship to number of "designated" Shares held
  - Type of units
  - Quality/Standards.
  - Compliance with Production Protocols (eg: for specialty markets such as E.U.)
  - Dates and frequency of sales (timing may be important for producers and NCG to meet processing/marketing objectives)
- Delivery:
  - Transportation costs
- Ability to Make Additional Deliveries:
  - In addition to Pre-Contracted Sales
  - Terms
- Acceptance/Rejection:
  - Right to Inspect
  - Right to Reject Product Not Up To Standard
  - Removal of Rejected Product
- Payment:
  - May Be Fixed to Published Rates
  - May be Split
- Damages/Remedies for Non-Delivery:
  - Right to Replace Delivery Shortfalls From Other Sources

- Liability For Losses

- Obligation to Accept Delivery:
  - Define When Obligation to Accept Delivery Excused (eg: Events Beyond NCG's Control)
  - Remedy for Non-Acceptance
- Dispute Resolution: - Arbitration/Mediation re: Price/Grades, etc.
- Termination: - Notice Provisions
- Assignment: - With Approved Transfer of "Designated" Shares

2. **Legal Issues**

- Not Enforceable Unless Clear (Certainty of Terms), Must be in Writing, Signed.

3. **Business Issues**

- As Clear, Short and Simple As Possible
- Understandable by Both Parties
- Fair to Both Sides
- Economically Attractive to Producer
- Must Permit Long Term Viability of NCG:
  - With this Guaranteed Supply of Product Will the NCG Meet Expenses and Make Money?

4. **Patronage Dividends/Reserves (Bylaws)**

- "Profit" to Members Based on Sales/designated Shares Held
- Provision for Reserves
- Provision for Loans

G. CONTINUANCE

1. General

- Existing Cooperatives Must Apply For Continuance Under the New Act by March 31, 2005.

- Cooperatives Which Do Not Continue Will Be Dissolved.

2. Continuance Procedure

- Submit Application to Cooperatives' Director Containing the Following:

  - Articles of Incorporation Under New Act

  - Directors' Declaration That Cooperative Will Be Organized, Operated and Carry On Business on a Cooperative Basis

  - If Continued as an NCG, a Directors' Declaration That It Will Comply with Part 18, Division 4 of the Act (the NCG Division)

  No Fee is Required

- On Acceptance of Application a Certificate of Continuance Will Be Issued

3. Post-Continuance

- The Continued Cooperative Must, Within One Year of the Certificate of Continuance, or By the Next Annual Members' Meeting, Pass New Bylaws Which Comply With the New Act and Regulations

H. <u>GOVERNANCE/CONTROL ISSUES</u>

1. **The Role of the Board of Directors**

   - all management decisions, subject to bylaws and unanimous agreement

2. **Member Elected Directors (Minimum 60%)**

   - one member on vote

3. **Investor Elected Directors (Maximum 20%)**

   - vote number of shares held

4. **Appointed Directors (Maximum 20%)**

   - significant "partners", community groups, investors, etc.

5. **Using Unanimous Agreements**

   - can be used to fundamentally change control of the NCG. Be careful.

6. **Because Members Usually "Control" the Management of NCG by Electing the Board**

   - consider restricting members to <u>only</u> those producers who:

     (a) make a significant financial contribution through acquisition of "designated" shares,

     (b) are clearly able to meet delivery obligations.

   - consider affording others (broader community) ability to participate through acquisition of investor shares.

   - carefully consider who you want to control the Board (eg: producers or investors); be mindful of potential issues arising from dilution of membership.

Resources

Christopher D. Merrett M., Holmes J., Eggert B. , Directory of Closed-Membership Producer Co-operatives: New Generation Co-operatives and Limited Liability Companies in the United States and Canada, Illinois Institute for Rural Affairs, June 2007.

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